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**To:** cserrano@hacienda.gobierno.pr; Glenn Cogswell (TAX); bjaskille@pridco.com; jramirez@pridco.com; mrobert@pridco.com  
**CC:** Cesar A. Gomez  
**Sent:** 4/12/2005 3:59:36 PM  
**Subject:** #541417 v1 - microsoft.mou.version2.markup  
**Attachments:** blrd01!.DOC

Dear all,

Attached is the final draft of the Microsoft MOU. If everyone is in agreement, please proceed to execute the same in counterparts. I will send messengers to PRIDCO and to Treasury to pick up an executed copy by each.

Thank you all for your cooperation.

Best regards,

Juni

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**Government  
Exhibit**

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MEMORANDUM OF UNDERSTANDING

THIS MEMORANDUM OF UNDERSTANDING is entered into by and among the Secretary of the Treasury of Puerto Rico (the "Secretary"), the Executive Director of Puerto Rico Industrial Development Company (the "Executive Director"), Microsoft Corporation ("Microsoft"), Microsoft Puerto Rico, Inc. ("MSPR"), and Microsoft Operations Puerto Rico LLC ("PR Newco").

The purpose of this Memorandum of Understanding is to set forth the tax regime that shall apply in connection with the establishment of PR Newco, a corporation to be organized by Microsoft under the laws of Puerto Rico, and with the integration, transition or migration of operations from MSPR to PR Newco.

WHEREAS, PR Newco will introduce to Puerto Rico new technologies and functions, including editing, pre-mastering and mastering of software codes into compact disk ("CD") and digital video disk ("DVD") formats, and the production of glass masters and stampers, with internal HEPA clean class 100 environment for media recording, encoded blue solid state recording laser ("BBSL"), and highly specialized micro-engineering processes.

WHEREAS, additional equipment to be installed by PR Newco in Puerto Rico will include three cells of electroforming galvanic.

WHEREAS PR Newco will introduce to Puerto Rico highly specialized micro-engineering processes.

WHEREAS, PR Newco will introduce to Puerto Rico DVD 9 format which provides increased storage capacity (CD 0.64 GB vs. DVD 8.5 GB), with two data substrate layers made of polycarbonate material with embedded digital code, bonded during a downstream process, labeled with off set or silkscreen printing, improved production capacity, and integrated in-line process which includes statistical monitoring tools.

WHEREAS, PR Newco will introduce edge-to-edge ("E2E") hologram-based anti-piracy ("AP") technology used to label Microsoft programs to provide unique hologram artwork through an embossing process.

WHEREAS, PR Newco will be the only authorized Microsoft E2E/DVD replication facility in the United States region.

WHEREAS, in 2007 PR Newco will introduce Key on Media, the most bullet-proof technology to increase AP security level on media level which will provide the capability to write up to 512 characters on media for improved security solutions.

WHEREAS, Key on Media uses Class-IV laser which ablates the reflective metal layer of the normal post-gap area of the optical media.

WHEREAS, PR Newco will introduce unique media serialization (product identification, product description and unique tracing capabilities).

WHEREAS, Microsoft will move the tasks from several locations in the United States to PR Newco, including some or all of the following:

Americas operations center forecasting and planning  
 Vendors contracts negotiation  
 Incremental offload processing and management  
 Vendors orders processing,  
 Glass mastering and hologram variants procurement  
 Americas operations center production capacity control  
 Quality management center

WHEREAS, PR Newco will be generating 46 additional full time jobs in Puerto Rico, including:

Operations management  
 Compliance management  
 Tax and finance analysis  
 Forecasting and planning  
 Supply chain management  
 Vendor management and contracts  
 Mastering process  
 Off-loading  
 Production/line workers

WHEREAS, PR Newco estimates that it will invest in excess of \$50 million in the construction and establishment of new facilities in Puerto Rico, and that said investment will be completed within 1 year from commencement of operations.

WHEREAS, PR Newco's estimated revenues for fiscal years 2007 through 2010 are as follows:

<u>Year</u>	<u>Revenue</u>
2007	\$4.0 billion
2008	\$4.2 billion
2009	\$4.8 billion
2010	\$5.2 billion
2011	\$5.4 billion
2012	\$5.6 billion

WHEREAS, PR Newco's estimated royalty payments for the above are:

<u>Year</u>	<u>Royalty Payment</u>
2007	\$2.2 billion
2008	\$2.3 billion
2009	\$2.7 billion
2010	\$2.9 billion
2011	\$3.0 billion
2012	\$0.3 billion

WHEREAS, MSPR is grantee of industrial tax exemption in Case No. 01-135-I-25, issued pursuant to the Tax Incentives Act of 1998, as amended (the "Act").

WHEREAS, Microsoft proposes that the operations of MSPR will integrate, transition or migrate from MSPR to PR Newco.

NOW, THEREFORE, the parties to this Memorandum of Understanding hereby agree to as follows:

1. The Secretary and the Executive Director shall favorably recommend to the Secretary of State of Puerto Rico the issuance and approval of a new grant of industrial tax exemption to MSPR and PR Newco (the "New Grant") pursuant to the provisions of the Act. A draft of the New Grant is attached herein for discussion purposes only which does not constitute a binding commitment or agreement of the parties hereto until and after being reviewed and agreed to by the Secretary, the Executive Director and the Secretary of State of Puerto Rico.
2. The essential terms of the New Grant shall be as follows:
  - (i) The New Grant shall provide that the grantees thereunder shall be MSPR and PR Newco.
  - (ii) The New Grant shall cover, pursuant to Sections 2(d)(1) and 2(i)(2) of the Act, the production and sale of computer software on any media, including but not limited to: (I) diskettes ("Diskettes"), (II) CDs-read only memory ("CD-ROMs"), (III) CDs-recordable ("CD-Rs"), and (IV) DVDs.
  - (iii) The New Grant shall provide that its effective date shall be April 1, 2005.
  - (iv) The New Grant shall provide for one or more tax exemption periods of at least 15 years in view of the location of MSPR and PR Newco in Humacao, Puerto Rico, and/or in another municipality in Puerto Rico to which at least a 15 year tax



exemption period has been assigned, pursuant to Section 6(d) of the Act.

- (v) The New Grant shall provide that MSPR and PR Newco shall constitute a core pioneer industry with new and innovative technology that has not been used in Puerto Rico prior to January 1, 2000, as contemplated in Section 3(a)(1)(A) of the Act.
- (vi) The New Grant shall provide: (A) that the fixed income tax rate applicable with respect to the net industrial development income ("IDI") derived by MSPR and PR Newco from the production and sale of computer software programs on Diskettes, CD-ROMs and CD-Rs shall be 2%, pursuant to Section 3(a)(1) of the Act; and (B) that the fixed income tax rate applicable with respect to the net IDI derived by MSPR and PR Newco from the production and sale of computer software programs on DVDs, and on any future media that qualifies under Section 3(a)(1)(A) of the Act, shall be 0%, pursuant to Section 3(a)(1)(A) of the Act. The New Grant shall further provide that any income or gain derived by MSPR or PR Newco from loans or other extensions of credit issued to other entities, including Microsoft affiliates, not engaged in trade or business in Puerto Rico, shall be treated as IDI derived by MSPR or PR Newco from the production and sale of computer software programs on Diskettes, CD-ROMs and CD-Rs, pursuant to Section 3(a)(1) of the Act. The New Grant shall also provide that, prior to the time when the new facilities are operational, the net income derived by MSPR or PR Newco as royalties relating to products covered by the New Grant shall be treated as IDI derived by MSPR or PR Newco, and that said IDI shall be subject to tax at the fixed income tax rate of 2%, pursuant to Sections 2(a)(3) and 3(a)(1) of the Act.
- (vii) The New Grant shall provide that the fixed income tax rate of 0% applicable with respect to the net IDI derived by MSPR and PR Newco from the production and sale of computer software programs on DVDs and other future media shall have an initial term of 5 years, which term may be renewed for an additional term of 5 years, pursuant to Section 3(a)(1)(B) of the Act, provided that the other future media complies with the provisions of Section 3(a)(1)(A) of the Act.

- (viii) The New Grant shall provide that in case of unanticipated or "extraordinary circumstances" (as said term is defined in Section 2(n) of the Act), including unexpected market demand for product, when MSPR or PR Newco may not be able to satisfy product demand, MSPR and PR Newco shall be allowed to contract the production of products outside Puerto Rico, and that the net income derived by MSPR and PR Newco from the sale of said products shall be subject to the fixed income tax rates set forth above for Diskettes, CD-ROMs, CD-Rs, and DVDs.
- (ix) The New Grant shall provide that during the period of integration, transition or migration of operations from MSPR to PR Newco, the income which will be subject to income and municipal license taxes in Puerto Rico shall not exceed the portion of the combined taxable income allocable to MSPR under Section 936(h)(5)(C)(ii) of the United States Internal Revenue Code of 1986, as amended.
- (x) The New Grant shall provide, with respect to IDI accumulated under the Act, that dividend and liquidating distributions made by MSPR or PR Newco shall not be subject to income tax, including income tax withheld at source, as provided in Sections 7(a) and 10(a) of the Act.
- (xi) The New Grant shall provide for an income tax rate of 2% on payments of royalties made by MSPR or PR Newco to any entities that are not engaged in trade or business in Puerto Rico, as provided in Section 6(k) of the Act.
- (xii) The New Grant shall provide for 90% exemption from personal and real property taxes, pursuant to Section 6(a) of the Act.
- (xiii) The New Grant shall provide for 60% exemption from municipal license tax, pursuant to Section 6(b)(1) of the Act.
- (xiv) The New Grant shall provide for 100% exemption from municipal construction taxes, as provided in Section 6(b)(4) of the Act.
- (xv) The New Grant shall provide for an employment requirement of 132 persons within 1 year from date of completion of construction and operation of the new facilities, subject to adjustments in the event of unforeseen circumstances or events.

- (xvi) The New Grant shall incorporate by reference all other benefits generally provided under the Act.
  - (xvii) The New Grant shall provide that MSPR and PR Newco shall be authorized to use in common major and minor facilities and personnel, pursuant to Section 2(h)(2) of the Act.
  - (xviii) The New Grant shall provide that MSPR shall not be considered a "predecessor exempted business", and that PR Newco shall not be considered a "successor business", for purposes of Section 11 of the Act. Accordingly, the New Grant shall provide that PR Newco shall be authorized to use all property previously used by MSPR.
  - (xix) The New Grant shall provide that its terms shall survive any amendment, modification, change, or repeal of any statute or regulation, pursuant to Section 13(f) of the Act.
3. The Secretary agrees that he will enter into a closing agreement with Microsoft, MSPR and PR Newco incorporating the terms of this Memorandum of Understanding to the extent that such terms are not included as part of the New Grant.
4. This Memorandum of Understanding may be signed in any number of counterparts, all of which shall constitute an entire agreement.

IN WITNESS WHEREOF, the parties hereto execute this Memorandum of Understanding on the \_\_\_\_ day of April, 2005.

Secretary of the Treasury of  
Puerto Rico

Executive Director of  
Puerto Rico Industrial  
Development Company

By: \_\_\_\_\_

By: \_\_\_\_\_

Microsoft Corporation

Microsoft Puerto Rico, Inc.

By: \_\_\_\_\_

By: \_\_\_\_\_

Microsoft Operations Puerto Rico LLC

By: \_\_\_\_\_



Attachment 1

GOVERNMENT OF PUERTO RICO  
DEPARTMENT OF STATE  
OFFICE OF INDUSTRIAL TAX EXEMPTION

Grant of Industrial Tax Exemption to MICROSOFT PUERTO RICO, INC. (hereinafter sometimes referred to as "MSPR") and MICROSOFT OPERATIONS PUERTO RICO, LLC (hereinafter sometimes referred to as "PR Newco") (together hereinafter referred to as the "applicants" or the "grantees"), Case No. 05-135-I-\_\_\_, pursuant to the provisions of Act No. 135 of December 2, 1997.

DECREE

WHEREAS, Act No. 135 of December 2, 1997, as amended (hereinafter the "Act"), empowers the Secretary of State of Puerto Rico to grant tax exemption from specified taxes to eligible businesses when it is proven to the satisfaction of the Secretary of State of Puerto Rico, that the applicants have established, or will establish an eligible business as this is defined in the Act, and that the same will be in the best interests of the Government of Puerto Rico;

WHEREAS, the Secretary of State of the Government of Puerto Rico, after having examined the findings of fact and conclusions of the Special Examiner, the report of the Director of the Office of Industrial Tax Exemption, and other documents relative to this case, is of the opinion that the applicants have proved that it will operate an eligible business within the meaning of the Act and that the same will be in the best interests of the Government of Puerto Rico;

WHEREAS, PR Newco will introduce to Puerto Rico new technologies and functions, including editing, pre-mastering and mastering of software code into compact disk ("CD") and digital video disk ("DVD") formats, and the production of glass masters and stampers, with internal HEPA clean class 100 environment for media recording, encoded blue solid state recording laser ("BBSL"), and highly specialized micro-engineering processes;

WHEREAS, additional equipment to be installed by PR Newco in Puerto Rico will include three cells of electroforming galvanic;

WHEREAS PR Newco will introduce to Puerto Rico highly specialized micro-engineering processes;

WHEREAS, PR Newco will introduce to Puerto Rico DVD 9 format which provides increased storage capacity (CD 0.64 GB vs. DVD 8.5 GB), with two data substrate layers made of polycarbonate material with embedded digital code, bonded during a downstream process, labeled with off set or silkscreen printing, improved production capacity, and integrated in-line process which includes statistical monitoring tools;

WHEREAS, PR Newco will introduce edge-to-edge ("E2E") hologram-based anti-piracy ("AP") technology used to label Microsoft programs to provide unique hologram artwork through an embossing process;

WHEREAS, PR Newco will be the only authorized Microsoft E2E/DVD replication facility in the United States region;

WHEREAS, in 2007 PR Newco will introduce Key on Media, the most bullet-proof technology to increase AP security level on media level which will provide the capability to write up to 512 characters on media for improved security solutions;

WHEREAS, Key on Media uses Class-IV laser which ablates the reflective metal layer of the normal post-gap area of the optical media;

WHEREAS, PR Newco will introduce unique media serialization (product identification, product description and unique tracing capabilities);

WHEREAS, Microsoft will move the tasks from several locations in the United States to PR Newco, including some or all of the following:

Americas operations center forecasting and planning  
Vendors contracts negotiation  
Incremental offload processing and management  
Vendors orders processing,  
Glass mastering and hologram variants procurement  
Americas operations center production capacity control  
Quality management center

WHEREAS, PR Newco will be generating 46 additional full time jobs in Puerto Rico, including:

Operations management  
Compliance management  
Tax and finance analysis  
Forecasting and planning  
Supply chain management  
Vendor management and contracts  
Mastering process  
Off-loading

Production/line workers

WHEREAS, PR Newco estimates that it will invest in excess of \$50 million in the construction and establishment of new facilities in Puerto Rico, and that said investment will be completed within 1 year from commencement of operations;

WHEREAS, PR Newco's estimated revenue for fiscal year 2007 is \$4.0 billion and its estimated royalty payments for that year are \$2.2 billion;

WHEREAS, MSPR is grantee of industrial tax exemption in Case No. 01-135-I-25, issued pursuant to the Act;

WHEREAS, Microsoft Corporation proposes that the operations of MSPR will integrate, transition or migrate from MSPR to PR Newco;

NOW, THEREFORE, BE IT DECREED BY THE SECRETARY OF STATE OF PUERTO RICO, pursuant to Sections 2(d)(1), 2(d)(4) and 2(i)(2), that the applicants, Microsoft Puerto Rico, Inc. and Microsoft Operations Puerto Rico LLC, be granted tax exemption in accordance with the applicable terms of the Act, for the production and sale of computer software programs on any media, including, but not limited to: (a) diskettes (hereinafter "Diskettes"), (b) compact disks-read only memory (hereinafter "CD-ROMs"), (c) compact disks-recordable (hereinafter "CD-Rs"), and (d) digital video disks (hereinafter "DVDs"), subject that the operations shall be carried out substantially as described in the application;

BE IT FURTHER DECREED, that pursuant to Section 13(j)(6) of the Act, the Secretary of State of the Government of Puerto Rico hereby authorizes the Director of the Office of Industrial Tax Exemption to carry on administrative duties of all nature, related with grants of tax exemption, including the approval or denial of tax exemption grants for property devoted to industrial development, but excluding the authority to approve or deny tax exemptions grants to manufacturing or service units and any other duty specifically bestowed upon him by the Act;

BE IT FURTHER DECREED, that, the effective date of this grant is April 1, 2005, and, pursuant to Section 6(d) of the Act, the grantees shall be entitled to a tax exemption period of fifteen (15) years, in view of the location of the exempted business in the Municipality of Humacao or \_\_\_\_\_, Puerto Rico;

BE IT FURTHER DECREED, that except as specifically provided in this grant, no income taxes or municipal license taxes shall be assessed or imposed on the grantees with respect of any income or volume of business derived by the grantees;

(10/22)

BE IT FURTHER DECREED, that the grantees shall constitute a medullar pioneer industry with new and innovative technology that has not been used in Puerto Rico prior to January 1, 2000, as contemplated in Section 3(a)(1)(A) of the Act;

BE IT FURTHER DECREED, pursuant to Section 3(a) of the Act, that the fixed income tax rate applicable with respect to the net industrial development income ("IDI") derived by the grantees from the production and sale of computer software programs on Diskettes, CD-ROMs and CD-Rs shall be two percent (2%), pursuant to Section 3(a)(1) of the Act; provided, that the fixed income tax rate applicable with respect to the net IDI derived by the grantees from the production and sale of computer software programs on DVDs or any future media shall be zero percent (0%), pursuant to Section 3(a)(1)(A) of the Act; provided, that the aforementioned fixed income tax rates shall apply in lieu of any other income tax or income tax rate or rates; provided, that notwithstanding the dates on which this grant would otherwise expire, the fixed income tax rate of zero percent (0%) provided in this grant for the net IDI derived by the grantees from the production and sale of computer software programs on DVDs or any future media shall have an initial duration of five (5) years commencing on the date or dates specified by the grantees on a notice filed with the Office of Industrial Tax Exemption, with copies filed with the Puerto Rico Industrial Development Company and with the Department of the Treasury; provided, that said initial five (5) year period shall be extended or renewed for an additional five (5) year period upon the expiration of the initial five (5) year period; and provided, that unless said five (5) year periods are otherwise extended or renewed, upon the expiration of said five (5) year periods, the fixed income tax rate of two percent (2%) provided hereinabove shall apply with respect to the net IDI derived by the grantees from the production and sale of computer software programs on DVDs or any future media;

BE IT FURTER DECREED, that any income or gain derived by the grantees from loans or other extensions of credit issued to other entities, including Microsoft affiliates, not engaged in trade or business in Puerto Rico, shall be treated as IDI derived by the grantees from the production and sale of computer software programs on Diskettes, CD-ROMs and CD-Rs, pursuant to Section 3(a)(1) of the Act;

BE IT FURTHER DECREED, that, prior to the time when the grantees' new facilities are operational, the net income derived by the grantees as royalties relating to products covered by this grant shall be treated as IDI derived by the grantees, and said IDI shall be subject to tax at the fixed income tax rate of two percent (2%) provided in this grant for IDI derived from the production and sale of computer software programs on Diskettes,



CD-ROMs and CD-Rs, pursuant to Sections 2(a)(3) and 3(a)(1) of the Act;

BE IT FURTHER DECREED, that in case of unanticipated or "extraordinary circumstances" (as said term is defined in Section 2(n) of the Act), including unexpected market demand for product, when the grantees may not be able to satisfy product demand, the grantees shall be allowed to contract the production of products outside Puerto Rico, and the net income derived by the grantees from the sale of said products shall be treated as IDI and shall be subject to the fixed income tax rates set forth in this grant for the production and sale of computer software programs on Diskettes, CD-ROMs, CD-Rs, and DVDs, and any future media;

BE IT FURTHER DECREED, that during the period of integration, transition or migration of operations from one grantee to the other, the income which will be subject to income and municipal license taxes in Puerto Rico shall not exceed the portion of the combined taxable income allocable to Microsoft Puerto Rico Inc. under Section 936(h)(5)(C)(ii) of the United States Internal Revenue Code of 1986, as amended;

BE IT FURTHER DECREED, that with respect to IDI accumulated under the Act, dividend and liquidating distributions made by the grantees shall not be subject to income tax, including income tax withheld at source, as provided in Sections 7(a) and 10(a) of the Act;

BE IT FURTHER DECREED, that the grantees shall be authorized to use in common major and minor facilities and personnel, pursuant to Section 2(h)(2) of the Act;

BE IT FURTHER DECREED, that neither of the grantees shall be considered a "predecessor exempted business" or a "successor business", for purposes of Section 11 of the Act; provided, that the grantees shall be authorized to use all property previously used by Microsoft Puerto Rico Inc.;

BE IT FURTHER DECREED, that terms of this grant shall survive any amendment, modification, change, or repeal of any statute or regulation, pursuant to Section 13(f) of the Act;

BE IT FURTHER DECREED, that any income, gain, volume of business, or other amounts that are paid, attributed, assigned, allocated, or imputed to any affiliate of the grantees or to any other person, pursuant to the United States Internal Revenue Code or any comparable statute of any foreign jurisdiction, or pursuant to any arrangement, agreement or understanding with any affiliate or other person, including without limitation any royalty, cost sharing, profit split, or other similar or analogous payments, shall be deducted, removed and excluded from the grantees' income and volume of business; provided, that



the grantees and its affiliates shall not be subject to income tax or municipal license tax with respect to any such income, gain, volume of business, payments, or other amounts; and provided, that if any amounts, previously included in the grantees' income or volume of business, are attributed, assigned, allocated, or imputed to any affiliate of the grantees or to any other person pursuant to the United States Internal Revenue Code or any comparable statute of any foreign jurisdiction, or pursuant to any arrangement, agreement or understanding, said amounts shall be deducted, removed and excluded from the grantees' income and volume of business;

BE IT FURTHER DECREED, that the gross income and taxable income of the grantees for Puerto Rico tax purposes shall conform with the gross income and taxable income of the grantees for purposes of the United States Internal Revenue Code or any comparable statute of a foreign jurisdiction; provided, that any cost sharing, profit split, royalty, or other analogous, comparable, or equivalent payments, attributions, assignments, allocations, or imputations made from the grantees to any affiliates thereof in order to reflect the gross income and taxable income of the grantees or other affiliates for purposes of the United States Internal Revenue Code or any comparable statute of a foreign jurisdiction, shall be removed and excluded from, and shall reduce, the grantees' gross income, taxable income and volume of business for Puerto Rico tax purposes; and provided, that any such payments, attributions, assignments, allocations, or imputations that are made to other affiliates shall be one hundred percent (100%) exempt from income taxes, including income taxes withheld at source, and from municipal license taxes;

BE IT FURTHER DECREED, that any cost sharing, profit split, royalty, or other analogous, comparable or equivalent payments, attributions, assignments, allocations, or imputations, that are made by the grantees to any affiliates thereof pursuant to the United States Internal Revenue Code or any comparable statute of any foreign jurisdiction, shall be removed and excluded from the grantees' income and volume of business; and provided, that the grantees and its affiliates shall be one hundred percent (100%) exempt from income and municipal license taxes with respect thereto;

BE IT FURTHER DECREED, that if the income of any affiliate of the grantees were adjusted by any taxing authority (hereafter the "Adjustment"), and the Adjustment involved or implied an actual, deemed or implicit decrease or increase in the taxable income or volume of business of the grantees below or above the taxable income or volume of business previously determined by the grantees on a return or declaration, a correlative adjustment shall be made in order to reflect the effect of the Adjustment on the taxable income and volume of business of the grantees;

provided, that if the effect of the Adjustment were an actual, deemed or implicit decrease in the taxable income or volume of business of the grantees, the grantees shall be entitled to receive credit, without interest, for any excess income and municipal license taxes previously paid; provided, that the grantees shall be free to remit an amount equal to the Adjustment to the relevant affiliate without the imposition of any income or municipal license taxes, and including taxes withheld at source; provided, that if the effect of the Adjustment were an actual, deemed or implicit increase in the taxable income or volume of business of the grantees, the grantees shall show an amount equal to the Adjustment on an amended return or declaration, and shall pay the corresponding taxes, without the imposition of any interest, surcharges, penalties, or other additions; and provided, that this clause shall apply notwithstanding any otherwise applicable periods of limitations; and provided, that nothing in this clause shall be construed as a limitation of any benefits provided in Article 1042-7 of the Regulations issued under the Internal Revenue Code of 1994, as amended (hereinafter the "Code"), which article shall apply with respect to the grantees and its affiliates notwithstanding the references therein to Section 936 or other provisions of the United States Internal Revenue Code;

BE IT FURTHER DECREED, that an income tax rate of two percent (2%) shall apply on payments of royalties made by the grantees to any entities that are not engaged in trade or business in Puerto Rico, as provided in Section 6(k) of the Act; provided, that said tax rate shall apply in lieu of any other tax or tax rate provided by law; and provided, that no income tax, including income tax withheld at source, shall apply with respect to such payments of royalties if said royalties constitute income from sources without Puerto Rico pursuant to Section 1123(c)(4) of the Code;

BE IT FURTHER DECREED, that all other benefits generally provided under the Act are incorporated to this grant;

BE IT FURTHER DECREED, that pursuant to Sections 2(j)(3) and 3(a)(3) of the Act, the net income derived by the grantees from investments in eligible activities listed under Section 2(j) of the Act shall be totally exempt from any income tax or any other tax, including tollgate tax, and from municipal license tax, and that the securities evidencing said investments shall be totally exempt from Commonwealth and municipal property taxes;

BE IT FURTHER DECREED, that, pursuant to Sections 6(a) of the Act, the grantees shall be ninety percent (90%) exempted from property taxes on real and personal property used in the operations covered by this grant; provided, that such taxes shall be assessed, imposed, notified and administered according to the property tax law in effect as of the date of assessment and

imposition; and provided, that the property described in the third and fourth paragraphs of Section 6(a) of the Act shall be totally exempt from property taxes as provided therein;

BE IT FURTHER DECREED, that, pursuant to Section 6(a) of the Act, all intangible property of the grantees of the nature of a patent, production license, invention, formula, formulation, design, plan, technique, know-how, trademark, process, procedure or technology acquired, transferred, assigned or developed, in whole or in part, or resulting from or associated with the grantees' operations or businesses, and all stocks, bonds and other securities issued by foreign (including United States) corporations, shall be totally exempted from property taxes;

BE IT FURTHER DECREED, that, pursuant to Section 6(b) of the Act, the grantees shall be sixty percent (60%) exempted from municipal license taxes, license fees, municipal excise taxes, or other municipal taxes imposed by any law or by any ordinance of any municipality; provided, that the taxable portion of the grantees' total volume of business shall be subject to municipal license tax at the rate in effect on the date of the signature of this grant; and provided, that said municipal license tax rate shall apply notwithstanding any subsequent amendment to this grant to cover operations in another municipality or municipalities;

BE IT FURTHER DECREED, that this grant shall cover the grantees' activities relative to the warehousing, marketing, delivery and sale of products covered by this grant, whether said activities are carried out in Humacao or \_\_\_\_\_ or elsewhere in Puerto Rico; and that said activities, and the income, volume of business and property associated therewith shall be covered by this grant;

BE IT FURTHER DECREED, that pursuant to Section 6(a) of the Act, during the period of construction or expansion of facilities and/or installation of machinery and equipment, the property of the grantees directly related to such construction, expansion and/or installation shall be totally exempt from real and personal property taxes; provided, that the total exemption that is herein conferred shall end on the date notified by the grantees to the Office of Industrial Tax Exemption, the Department of the Treasury and the Municipal Revenues Collection Center (hereinafter the "MRCC") as the correct date on which the construction or expansion of facilities and/or installation of machinery and equipment was completed; provided that, with respect to any subsequent construction or expansion of facilities and/or installation of machinery and equipment, the grantees will enjoy the same total exemption provided above from real and personal property taxes;

BE IT FURTHER DECREED, that pursuant to Section 6(b)(4) of the Act, during the period of construction or expansion of any facilities, the grantees and their contractors and subcontractors shall be totally exempt from any tax, duty, license fee, excise, assessment or tariff imposed by any municipality on construction carried out within the municipality; provided, that the total exemption that is herein conferred shall end on the date notified by the grantees to the Office of Industrial Tax Exemption, the Department of the Treasury and the relevant municipality as the correct date on which the construction or expansion of facilities was completed; provided, that with respect to any subsequent construction or expansion of facilities, the grantees, and their contractors and subcontractors, shall enjoy the same total exemption provided in this clause; and provided, that any installation of new machinery and equipment by the grantees, or by their contractors and subcontractors, that is treated by a municipality as a construction or expansion of facilities, shall enjoy the same total exemption provided in this clause;

BE IT FURTHER DECREED, that changes, modifications, variations, substitutions or additions to the manufacturing process of the products, as well as the raw materials used in, the packaging of, and/or the machinery and equipment used for the production of, the products covered by this grant, as may be required by governmental, judicial or regulatory authorities, manufacturing or product standards, technological advances, market demands, material supplies, or any similar conditions, shall not affect the coverage of said products under this grant, provided that the grantees comply with the "industrial operations" requirement provided in Section 2(g) of the Act;

BE IT FURTHER DECREED, that pursuant to Section 11(a)(4) of the Act, the use by the grantees of physical facilities and other facilities, as described in said section, that have been previously used by Microsoft Puerto Rico, Inc. or by any other exempted business, is hereby authorized, and that the grantees shall not be considered a "successor business", as said term is defined in the Act, inasmuch as said use and the grantees' operations are in the best economic and social interest of Puerto Rico; and provided, that any said facilities shall be covered by this grant;

BE IT FURTHER DECREED, that the provisions of Section 11(b)(3) of the Act be waived in view of the fact the grantees' operations are in the best interests of the economic and social welfare of Puerto Rico, in consideration of the nature of the physical facilities, the number of jobs, the amount of payroll, the total investment and the nature of the project;

BE IT FURTHER DECREED, that pursuant to Sections 2(h)(1) and 2(h)(2) of the Act, the grantees shall be allowed full use in



common of minor and major facilities and personnel between or among all the operations covered by this grant;

BE IT FURTHER DECREED, that all the credits and deductions contained in the Act shall be applicable with respect to the grantees;

BE IT FURTHER DECREED, that the grantees must comply with all the laws, rules, regulations, orders and ordinances promulgated by the Government of Puerto Rico, its Agencies and Municipalities which are applicable to grantees' operations;

BE IT FURTHER DECREED, that the grantees shall make all possible efforts to buy from local manufacturers all products, components, equipment, machinery and materials necessary for its operations;

BE IT FURTHER DECREED, that this grant of tax exemption shall be null and void retroactively, unless the grantees file with the Office of Industrial Tax Exemption, within ninety (90) days subsequent to the date of receipt of this grant, a sworn statement in which the grantees state the unconditional acceptance of this grant and of all the conditions, provisions and determinations which form an integral part of the same;

BE IT FURTHER DECREED, that as an essential condition to the issuance and continuance of this grant, grantees must maintain an annual average minimum employment of 132 persons, within one year from the date of completion of construction and operation of the new facilities, in the activities covered by this grant, and must continue to so directly employ at least said number of persons in its locations;

BE IT FURTHER DECREED, that the grantees must always comply with the employment requirement indicated in the above clause, except in cases of unforeseen circumstances, which may cause a reduction of employment beyond the control of the grantees, at which occurrence or at the earliest date when such occurrence is contemplated, the grantees shall be subject to one of the following alternatives:

1. If the reduction represents less than 10% of the employment requirement, grantees shall have no obligation to notify the Office of Industrial Tax Exemption of said reduction;

2. If the reduction represents 10% or more but less than 25% of the employment requirement, grantees shall notify, within thirty (30) days of such reduction occurs, to the Office of Industrial Tax Exemption, with copies to the Department of Labor and Human Resources of Puerto Rico and to the Puerto Rico Industrial Development Company, of



said reduction of employees on a sworn statement sent by certified mail with return receipt requested, or in the alternative, shall file said sworn statement personally at the Office of Industrial Tax Exemption with copy to the Department of Labor and Human Resources of Puerto Rico and the Puerto Rico Industrial Development Company;

3. If the reduction represents 25% or more of the employment requirement, grantees must file, within thirty (30) days of such reduction occurs, to the satisfaction and acceptance, which acceptance shall not be unreasonably withheld, with the Office of Industrial Tax Exemption a sworn application, with copies to the Department of Labor and Human Resources of Puerto Rico and the Puerto Rico Industrial Development Company, requesting approval of the Office of Industrial Tax Exemption for said reduction; PROVIDED, that the Office of Industrial Tax Exemption shall make a written determination within sixty (60) days of the date of receipt and acceptance of such application as to whether the grantees shall be deemed to be in compliance with the employment requirement taking into consideration such reasonable grounds for reduction of employment, as for example, but not limited to, strikes, war, action of a government or the elements, or any extraordinary circumstances, as such term is defined in Section 2(n) of the Act, and if the grantees are not given notice of such determination by the Office of Industrial Tax Exemption within said sixty (60) days, the grantees shall without further action or formality, be deemed to be in compliance with such employment requirement; provided, further, that it may in lieu of cancellation of the decree in those cases in which the reduction of 25% or more of the employment requirement is not approved:

a) increase the fixed income tax rate and reduce the rate of tax exemption proportionately in a ratio which bears the relation between the reduced employment to the employment requirement; and/or

b) approved a temporary reduction of the employment requirement when the circumstances so merit by negotiating any other reasonable condition satisfactory both to the grantees and the Government of Puerto Rico, and, a waiver of the employment requirement will be granted when in the judgment of the pertinent Government agencies such terms of the negotiation further the purposes of industrial development under this Act;

BE IT FURTHER DECREED, that the grantees shall have the right to take into account, for purposes of the minimum employment requirement, temporary persons rendering services as an employee in any of the operations covered by this grant,

regardless whether said persons are not directly on the payroll of the grantees (such as persons under leasing of employees contracts), but excluding third party consultants and independent contractors that carry out activities that are not commonly realized by the grantees in their operations;

BE IT FURTHER DECREED, that the minimum employment requirement contained in this grant shall be subject to adjustments in the event of unforeseen circumstances or events; provided, that in the event that any decrease in demand for Diskettes, CD-ROMS, CD-Rs, or DVDs occurs, said minimum employment requirement shall be adjusted to the actual number of persons required by the grantees to produce its products and meet the demand of said products; and provided, that the grantees shall notify said actual number of persons to the Office of Industrial Tax Exemption;

BE IT FURTHER DECREED, that the grantees shall make all possible efforts to hire its production workers from the unemployed labor force listed in the Employment Service Division of the Bureau of Employment Security of the Department of Labor and Human Resources of the Government of Puerto Rico;

BE IT FURTHER DECREED, that the continuance of this grant of tax exemption shall be conditional upon compliance by the grantees with such regulations and requirements as the Environmental Quality Board of the Government of Puerto Rico has heretofore promulgated and may hereafter promulgate, relative to the control of water, air, ground and any other environmental pollution, and which may be applicable to the manufacturing operations of the grantees;

BE IT FURTHER DECREED, that the benefits granted herein shall be applicable only to the property used in connection with the operations hereinbefore listed and the fixed tax rate to the industrial development income (as defined in the Act) derived from the operations which give rise to the exemption provided by this decree, and such other property specifically declared exempt by the Act;

BE IT FURTHER DECREED, that this grant shall include exemption to the extent provided in the Act from all Puerto Rico taxes, and from license fees and other municipal taxes levied by any ordinance of any municipality, except as otherwise hereinbefore or after provided in this decree;

BE IT FURTHER DECREED, that there shall be excluded from the scope of the benefits the operation of retail stores; all wholesale transactions other than the original sale at the factory price of the product manufactured; and, the providing of any services in connection with the sales of the products, except as otherwise hereinbefore provided;

BE IT FURTHER DECREED, that this grant shall not include exemption from:

- a. Workmen's compensation premiums as provided by law;
- b. Fees for motor vehicle licenses or plates;
- c. Taxes levied under Act No. 286, of April 6, 1946;
- d. License fees or excises levied under the Subtitle B of the Puerto Rico Internal Revenue Code, approved on October 31, 1994; provided, that the attention of the grantees hereof is called to the fact that it may avail itself, to the extent applicable and while in force or otherwise modified, of certain exemptions contained in the Subtitle B of the Puerto Rico Internal Revenue Code of Puerto Rico such as, among others, those contained in Section 2031 thereof;

BE IT FURTHER DECREED, that as a condition to the continuance of the tax benefit hereby granted the grantees shall be required, in conformance with Section 14 of the Act to file with the Secretary of the Treasury of the Government of Puerto Rico, regardless of its gross or net income, an annual income tax return, separate from any other return it is required to file, in relation to the business operations of the trade that is the object of the exemption and in accordance with the Internal Revenue Code of Puerto Rico, as amended (hereinafter the "Code"); the exempted business shall also be required to keep in Puerto Rico the accounting records relative to its operations separately, as well as the necessary records and files, and to make and submit such sworn statements and comply with the rules and regulations in force for the proper fulfillment of the purposes of the Code and that the Secretary of the Treasury of the Government of Puerto Rico may prescribe from time to time in connection with the levying and collection of all kinds of taxes; every exempted business shall file duly completed reports and surveys for the preparation of statistic and economic studies that from time to time may be requested by the Executive Director of the Puerto Rico Development Company in the performance of his duties; provided, further, that the grantees shall file duly completed reports that may be requested by the Office of the Commissioner of Financial Institutions;

BE IT FURTHER DECREED, that the Executive Director of the MRCC and the Secretary of the Treasury of the Government of Puerto Rico shall determine for each taxable year covered by this exemption what property and what income the grantees have used in, or derived from the industrial operations covered by this grant, PROVIDED, that nothing contained herein shall deprive the grantees of their right to administrative and judicial review of such determinations of the Executive Director of the MRCC and the

Secretary of the Treasury of the Government of Puerto Rico available by Constitution, Law or Regulations;

BE IT FURTHER DECREED, that the Executive Director of the MRCC and the Secretary of the Treasury of the Government of Puerto Rico, in determining what property and what income has been derived from the industrial operations of the grantees covered by this grant, may review the accounts and records of the grantees to determine that all purchase prices, sales prices, rates of lease, overhead or any other cost allocations and all other prices, rates, and cost allocations are fixed on the basis of normal business operations and not for the purposes of avoiding taxes ordinarily chargeable to activities not within the scope of the industrial operations covered by this grant or of charging to the operations carried on outside of Puerto Rico; PROVIDED, that wherever the Executive Director of the MRCC and the Secretary of the Treasury of the Government of Puerto Rico find that such rates or charges are made for the purposes of extending the coverage of the grant beyond the scope of the covered operations reasonable adjustments shall be made for the purpose of calculating the amount of taxes payable by the grantees, if any, and they shall make such recommendations to the Secretary of State as to such other action as may be taken under the provisions of Section 12(c)(1) of the Act and the Rules and Regulations promulgated thereunder; PROVIDED, that nothing contained herein shall deprive the grantees of their right to administrative and judicial review of such determination of the Executive Director of the MRCC and the Secretary of the Treasury of the Government of Puerto Rico available by Constitution, Law or Regulations;

BE IT FURTHER DECREED, that the grantees shall operate the business covered by this grant in good faith and in accordance with the principles of normal business operations, and shall not willfully attribute to the operations and accounts for the activities covered by this grant, activities carried on in Puerto Rico or any other place which are not part of the operations of the tax exempt business covered by this grant;

BE IT FURTHER DECREED, pursuant to Section 13(f) of the Act, that upon acceptance of this grant, the grantees recognize that they shall be required to comply with all the relevant provisions of the Act, and all rules and regulations promulgated by the Director of the Office of Industrial Tax Exemption and approved by the Governor and/or the Secretary of State in accordance with the provisions of Section 13(i) of the Act, regardless of whether or not said provisions are specifically mentioned in this grant of tax exemption; PROVIDED, however, that this decree shall upon its acceptance by grantees constitute a contract between the Government of Puerto Rico and the grantees;



BE IT FURTHER DECREED, that upon acceptance of this grant by the grantees, this grant of industrial tax exemption shall constitute a contract between the grantees, its stockholder(s), and the Commonwealth of Puerto Rico, and as such the provisions of this grant shall prevail over, and shall not be modified, diminished, impaired, or revoked by, any laws, regulations and/or interpretative pronouncements enacted, promulgated and/or issued by the government of the Commonwealth of Puerto Rico or any of its instrumentalities or political subdivisions, or by any municipality in Puerto Rico, and nothing shall modify, diminish, impair, or revoke the terms of this grant from and after the Effective Dates unless so elected and authorized by the grantees in writing;

BE IT FURTHER DECREED, pursuant to Section 13(f) of the Act, that no events subsequent to April 1, 2005, including without limitation any statute, law, regulation, judgment, determination, circular letter, bulletin, proclamation, pronouncement, edict, ordinance, decree, or other action enacted, promulgated, adopted, issued, or taken by the Government of Puerto Rico, or by any of its instrumentalities or political subdivisions, by any court or tribunal, or by any municipality or municipal body, and including without limitation the Office of the Commissioner of Municipal Affairs (in its Spanish acronym, "OCAM"), shall diminish, impair or adversely affect the terms of this grant, or the benefits granted hereunder, unless specifically authorized by the grantees in writing;

BE IT FURTHER DECREED, that upon receipt of this grant, the Director of the Office of Industrial Tax Exemption shall immediately forward a copy to the grantees.

MARISARA PONT MARCHESE  
SECRETARY OF STATE

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